No. 09-1

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

DEANNA McBREARTY and MARYLYNN HARTSEL, individually, derivatively, and on behalf of all others similarly situated,

Petitioners,

v.

THE VANGUARD GROUP, INC., GEORGE U. SAUTER, DUANE F. KELLY, JOHN J. BRENNAN, CHARLES D. ELLIS, RAJIV L. GUPTA, AMY GUTMANN, JOANN HEFFERNAN HEISEN, ANDRE F. PEROLD, ALFRED M. RANKIN JR., J. LAWRENCE WILSON, ACADIAN ASSET MANAGEMENT, LLC, RONALD D. FRASHURE, JOHN R. CHISHOLM, BRIAN K. WOLAHAN, MARATHON ASSET MANAGEMENT, LLP, NEIL M. OSTRER, VANGUARD INTERNATIONAL EQUITY INDEX FUNDS, d/b/a VANGUARD EUROPEAN STOCK INDEX FUND, and VANGUARD HORIZON FUNDS, d/b/a VANGUARD GLOBAL EQUITY FUND,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

Respondents are mutual fund managers who knowingly purchased stock in offshore gambling entities that illegally earned nearly 90% of their revenues from gamblers in the United States. The mutual funds suffered massive losses following law enforcement in the U.S. against the illegal gambling businesses that choked off their primary source of revenue and lead to the forfeiture of almost $650 million in criminal proceeds. Respondents' unlawful investments violated 18 U.S.C. § 1955 ("§ 1955"), which makes it illegal to "own all or part of an illegal gambling business." A violation of § 1955 is a predicate crime under the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961(1) ("RICO"). Petitioners sued on behalf of the mutual funds under RICO, alleging that the investment losses had been "the foreseeable, direct and natural consequences of [Respondents'] unlawful investments in illegal gambling businesses" and thus had been "proximately caused by [Respondents'] racketeering activities." The Court of Appeals for the Second Circuit affirmed the dismissal of Petitioners' RICO claims as a matter of law, holding that the complaint failed to allege proximate causation.

Three questions are presented:

1. Does a reasonably foreseeable intervening cause (in this case, government enforcement of criminal laws) sever proximate causation under RICO? The Court of Appeals held that it does. Under *Bridge v. Phoenix Bond & Indemnity Co.*, 553 U.S. 639, 128 S. Ct. 2131 (2008), it does not.

2. May lower courts dispense with the proximate cause enquiry required by *Holmes v. Sec. Investor Prot. Corp.*, 503 U.S. 258 (1992), in favor of a mechanical, black-letter rule that "proximate causation is lacking under RICO when the harm results from the exposure or disclosure of the RICO predicate activity"? The Court of Appeals accepted that all three *Holmes* factors weighed in Petitioners' favor and that Petitioners' injuries had been reasonably foreseeable consequences of Respondents' racketeering but nevertheless affirmed the dismissal of Petitioners' RICO claims.

3. Where the plaintiff alleges a direct "first step" injury not contingent on harm suffered by a third-party from the racketeering activity, does RICO impose a proximate cause requirement that is stricter than at common law? The Court of Appeals held that it does.

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OPINIONS BELOW

The order of the United States Court of Appeals for the Second Circuit entered November 23, 2009, appears in the appendix at pp. 1-5. It is not officially reported but is available on Westlaw. *McBrearty v. Vanguard Group, Inc.*, No. 09-1445-cv, 2009 WL 4019799 (2d Cir. Nov. 23, 2009).

The order of the Court of Appeals denying rehearing and rehearing *en banc* entered January 12, 2010, appears in the appendix at pp. 16-17 and is unreported.

The memorandum and order of the United States District Court for the Southern District of New York entered April 6, 2009, appears in the appendix at pp. 6-15. It is not officially reported but is available on Westlaw. *McBrearty v. Vanguard Group, Inc.*, No. 08 Civ. 7650, 2009 WL 875220 (S.D.N.Y. Apr. 2, 2009).

JURISDICTION

The Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

The order sought to be reviewed was entered on November 23, 2009. The order denying rehearing was entered January 12, 2010.

The District Court possessed subject matter jurisdiction under 28 U.S.C. § 1331 (federal question), 1337 (commerce regulation), and 1367(a) (supplemental jurisdiction) and under 18 U.S.C. § 1964 (RICO).

The Court of Appeals possessed appellate jurisdiction pursuant to 28 U.S.C. § 1291 (final decision). Final judgment was entered on April 6, 2009. Petitioners timely filed their notice of appeal to the Court of Appeals on April 8, 2008.

STATUTES INVOLVED

18 U.S.C. § 1964(c) provides, in pertinent part:

> Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therefor in any appropriate United States district court . . . .

18 U.S.C. § 1962(c) provides:

> It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

18 U.S.C. § 1961(1) provides, in pertinent part:

> "racketeering activity" means . . . (B) any act which is indictable under any of the following provisions of title 18, United States Code: . . . section 1955 . . . .

18 U.S.C. § 1955(a) provides:

Whoever conducts, finances, manages, supervises, directs, or owns all or part of an illegal gambling business shall be fined under this title or imprisoned not more than five years, or both.

18 U.S.C. § 1955(b)(1) provides:

> "illegal gambling business" means a gambling business which—
>
> > (i) is a violation of the law of a State or political subdivision in which it is conducted;
> >
> > (ii) involves five or more persons who conduct, finance, manage, supervise, direct, or own all or part of such business; and
> >
> > (iii) has been or remains in substantially continuous operation for a period in excess of thirty days or has a gross revenue of $2,000 in any single day.

STATEMENT OF THE CASE

Petitioners are investors in two Vanguard mutual funds. Respondents, the fiduciaries who managed and advised the funds, knowingly caused the funds to make substantial investments in offshore Internet gambling entities whose principal source of revenue was from gamblers in the U.S., in violation of U.S. anti-gambling laws.[1] The foreign gambling companies were "illegal gambling businesses" as that term is defined in § 1955(b). They and their principals have since forfeited to the federal government almost $650 million in criminal proceeds. Their founders have pleaded guilty to criminal offenses subjecting them to significant fines and prison sentences.

Section 1955(a) provides that whoever "owns all or part of an illegal gambling business" is guilty of a felony. By causing the mutual funds to purchase stock in illegal gambling businesses, Respondents caused the mutual funds to own part of such businesses in violation of § 1955. A violation of § 1955 is a predicate crime under RICO. 18 U.S.C. § 1961(1). By purchasing shares in illegal gambling businesses repeatedly and over a significant period of time, Respondents conducted the affairs of the mutual funds through a "pattern of racketeering" in violation of RICO. 18 U.S.C. § 1962(c).

In making the unlawful investments, Respondents took a reasonably foreseeable risk that the mutual funds

1. The mutual funds on whose behalf Petitioners sue are nominal defendants and respondents, but they are not included within the term "Respondents" as used in this Petition.

would suffer losses should law enforcement authorities prosecute and force the illegal gambling businesses to stop violating U.S. anti-gambling laws. The gambling companies *actually warned* Respondents in their prospectuses that they violated U.S. criminal statutes. For example, one of the foreign gambling companies disclosed to Respondents that "the US Department of Justice considers that companies offering online gaming to US residents are in violation of existing US federal laws," but Respondents invested anyway. The same gambling company explicitly warned Respondents that law enforcement "could result in investors losing all or a very substantial part of their investment." That is exactly what happened. Following a law enforcement crackdown spearheaded by the United States Department of Justice aimed at illegal Internet gambling, the mutual funds suffered significant investment losses as the share prices of the foreign gambling entities plummeted in the foreign markets in which they traded to reflect the loss of their primary source of revenue.*

Petitioners brought this derivative action under RICO, on behalf of the mutual funds, to recover for the investment losses that the mutual funds suffered as the direct and reasonably foreseeable result of Respondents' unlawful investments in illegal gambling businesses.

The District Court dismissed Petitioners' RICO claims for failure to allege proximate causation. Disregarding the three factors relied on by the Court in *Holmes* and its progeny, the District Court held that (i) the mutual funds' investment losses had been proximately caused not by Respondents' illegal investments, but rather by the "intervening" actions of the government in enforcing anti-gambling and racketeering laws; and (ii) Petitioners "were not the intended victims or targets" of Respondents' racketeering activities. (14a)

* The shares were not traded in the U.S. due to the illegality.

The Court of Appeals for the Second Circuit affirmed, saying:

> [t]he decline in the funds' online gambling holdings was not the direct result of the RICO violation – the owning and/or financing of illegal gambling – but rather was the result of the subsequent "government crackdown" on the illegal gambling. Although plaintiffs contend that the law enforcement crackdown was a foreseeable risk of defendants' activities (rather than a supervening cause), we have already held that proximate causation is lacking under RICO when the harm results from the exposure or disclosure of the RICO predicate activity. *In re Am. Express Co. S'holder Litig.*, 39 F.3d 395, 400 (2d Cir. 1994).

(4a)

In a footnote, the Court of Appeals held that RICO proximate causation is more demanding than what is required at common law, so as to render foreseeability immaterial:

> Although foreseeability is often the test of proximate causation at common law, *see Palsgraf v. Long Island R.R. Co.*, 162 N.E. 99, 100 (N.Y. 1928), RICO causation is a concept distinct from "proximate causation as that term is used at common law." *Abrahams v. Young & Rubicam Inc.*, 79 F.3d 234, 237 (2d Cir. 1996).

(4a n.1)

Like the District Court, the Court of Appeals also refused to conduct the proximate cause inquiry using the three factors relied on by the Court in *Holmes*. Neither the District Court nor the Court of Appeals has ever identified even a single *Holmes* factor that weighs against a finding of proximate causation in this case. Nevertheless, the Court of Appeals held that "even assuming *arguendo* that [the *Holmes*] policy considerations cut in plaintiffs' favor, they cannot remedy the basic defects in causation . . . ." (4a)

REASONS FOR GRANTING THE PETITION

I. The Writ of Certiorari Should Be Granted to Determine Whether Reasonably Foreseeable Intervening Events Insulate Racketeers from Civil Liability Under RICO

The Court of Appeals refused to consider basic common law principles in evaluating the significance of intervening causes under RICO and thus decided an important question of federal law contrary to the relevant decisions of the Court. Sup. Ct. Rule 10(c). The decision below also conflicts with the decisions of other Courts of Appeals on the same important matter. Sup. Ct. Rule 10(a). The undisputed facts of this case also afford an opportunity for the Court to resolve legal issues left unsettled by *Hemi Group, LLC v. City of New York*, 130 S. Ct. 983 (Jan. 25, 2010).

In *Bridge v. Phoenix Bond & Indemnity Co.*, 553 U.S. 639, 128 S. Ct. 2131 (2008), the Court held that defendants' racketeering activities proximately caused the plaintiffs' RICO injuries even though contributing

causes – including government action – had intervened between the defendants' RICO violations and the plaintiffs' injuries. The plaintiffs and defendants in *Bridge* were competing buyers at a public auction. The defendants allegedly committed mail fraud by submitting false certifications to the government authorities conducting the auction. The false certifications misled government authorities concerning the identities of the defendants and the agents bidding on their behalf. The government authorities consequently awarded to the defendants a greater percentage of auction sales when the plaintiffs and defendants submitted equal bids. Despite the governmental action that had intervened between the defendants' fraud and the plaintiffs' injuries, the Court held that the RICO violations proximately caused the plaintiffs' injuries.

The Court said that the government's actions in permitting the defendants to participate in the auction had been the "foreseeable and natural consequence" of the fraud, 128 S. Ct. at 2144, and therefore had *not* been "an intervening cause breaking the chain of causation." *Id.* That holding is entirely consistent with well-established common law principles of causation.

At common law, certain intervening events – also called "superseding causes" – may sever the causal nexus between a defendant's wrongdoing and a plaintiff's injury. This occurs, however, only if the injury is neither reasonably foreseeable nor part of the risk created by a defendant's wrongful conduct. *See, e.g.*, *Exxon Co., U.S.A. v. Sofec, Inc.*, 517 U.S. 830, 837 (1996) ("'The doctrine of superseding cause is . . . applied where

. . . the injury was actually brought about by a later cause of *independent origin that was not foreseeable*'") (emphasis added)), *quoting* 1 T. Schoenbaum, *Admiralty and Maritime Law* § 5-3, pp. 165-166 (2d ed. 1994).

A later cause can supersede the original cause only if it is independent of the original cause. *See, e.g., Aetna Ins. Co. v. Boon*, 95 U.S. 117, 130 (1877). For a cause nearer in time to be an "independent" cause – or, to use the terminology of *Anza v. Ideal Steel Supply Corp.*, 547 U.S. 451, 458 (2006), for it to be "entirely distinct" so as to cut off liability – it must be neither reasonably foreseeable nor part of the risk created by the defendant's wrongful act. As Judge Friendly explained, "not every new force insulates a negligent defendant from liability or a plaintiff guilty of contributory fault from the consequences. The principle is limited to 'intervening causes which could not reasonably be foreseen, and which are no normal part of the risk created.'" *East Hampton Dewitt Corp. v. State Farm Mut. Auto. Ins. Co.*, 490 F.2d 1234, 1240 (2d Cir. 1973), *quoting* W. Keeton, D. Dobbs, R. Keeton & D. Owen, *Prosser and Keeton on Law of Torts* § 44, p. 281 (5th ed. 1984) [hereinafter *Prosser & Keeton*]. *Accord Bonsignore v. City of New York*, 683 F.2d 635, 638 (2d Cir. 1982), *quoting Derdiarian v. Felix Contracting Corp.*, 51 N.Y.2d 308, 316 (1980).

Not even the intentional or criminal act of a third-party is sufficient to break a causal chain where the intervening act is reasonably foreseeable. *See Lillie v. Thompson*, 332 U.S. 459, 462 (1947) (*per curiam*); *Hemi*, 130 S. Ct. at 998 (Breyer, *J.*, dissenting). *See also Preston*

v. Cauldwell-Wingate Co., 176 F.2d 237, 241 (2d Cir. 1949) (L. Hand, *J.*) ("it is not the law of New York that the intervention of a succeeding fault as such gives immunity to an earlier wrongdoer"); *Horan v. Watertown*, 217 Mass. 185, 186, 104 N.E. 464, 465 (1914).

Refusing to follow *Bridge* and established common law principles, the Court of Appeals held that, in the RICO context, even reasonably foreseeable intervening events – here, government enforcement of criminal statutes – are sufficient to insulate racketeers from civil liability. (4a) This was error. The refusal of the Court of Appeals to apply basic common law principles in determining whether an intervening event constitutes a "supervening cause" under RICO cannot be reconciled with *Bridge* or with decisions of other Courts of Appeals. *See, e.g., Mid Atlantic Telecom, Inc. v. Long Distance Servs., Inc.*, 18 F.3d 260, 263-64 (4th Cir. 1994) ("[t]aking the complaint at face value, it cannot be said that we are confronted with circumstances . . . where the intervening acts were wholly independent of the alleged [RICO] predicate acts."); *Cox v. Admin. United States Steel & Carnegie*, 17 F.3d 1386, 1399 (11th Cir. 1994) (where defendant's racketeering activity was a "substantial factor" in causing the harm, the existence of a contributing cause was "beside the point"), *citing Prosser & Keeton* § 41, at 268 ("If the defendant's conduct was a substantial factor in causing the plaintiff's injury, it follows that he will not be absolved from liability merely because other causes have contributed to the result, since such causes, innumerable, are always present").

By ignoring basic common law concepts, the decisions below effectively require that a RICO plaintiff's injury be caused by only one source. This conflicts with decisions of other Courts of Appeals. As the Eleventh Circuit has explained, "[i]n both federal RICO and federal antitrust cases, 'proximate cause is not . . . the same thing as sole cause,' and it is enough for the plaintiff to plead and prove that the defendant's tortious or injurious conduct was a 'substantial factor in the sequence of responsible causation.'" *Williams v. Mohawk Indus., Inc.*, 465 F.3d 1277, 1288 n. 5 (11th Cir. 2006), *citing Cox*, 17 F.3d at 1399. *See also, Oki Semiconductor Co. v. Wells Fargo Bank, Nat. Ass'n*, 298 F.3d 768, 773 (9th Cir. 2002) (relying on "substantial factor" test).

The Court's antitrust decisions confirm that reasonably foreseeable intervening events do not insulate a defendant from liability so long as the defendant's wrongdoing is a material cause of the plaintiff's injury.[2] In *Blue Shield of Virginia v. McCready*, 457 U.S. 465, 480 n.17 (1982), the Court found that a subsequent event that "contributed" to the plaintiff's injury did not break the sequence of responsible causation. Similarly, in *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 114 n. 9 (1969), the Court held that it is "enough that the illegality is shown to be a material cause . . . a plaintiff need not

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2. The Court often looks to antitrust precedent for guidance when addressing RICO issues. *See Holmes*, 503 U.S. at 272; *Anza*, 547 U.S. at 477 (Thomas, *J.*, concurring in part and dissenting in part); *Agency Holding Corp v Malley-Duff & Assoc's Inc*, 483 U.S. 143, 150 (1987).

exhaust all possible alternative sources of injury in fulfilling his burden of proving compensable injury under § 4 [of the Clayton Act]." *See Hasbrouck v. Texaco, Inc.*, 842 F.2d 1034, 1042-45 (9th Cir. 1987) (intervening causes did not break the chain of causation).

Given the weight of the foregoing authority, the question raised in dissent by Justice Breyer in *Hemi* is particularly apt here: Where "so much basic common law argues in favor of [a finding that proximate cause exists], how can the Court avoid that conclusion here?" 130 S. Ct. at 998 (Breyer, *J., dissenting*).

Unless the Court clarifies the law in this area, the decision below will operate in this and other cases to insulate from liability defendants who inflict significant injury in violation of RICO.[3] While the Court may have hoped to clarify the law in this area when it granted certiorari in *Hemi*, that case failed to produce an

3. Other mutual fund managers who unlawfully invested in illegal offshore gambling businesses have successfully relied on the precedent of the decision below in their attempt to cut off recovery of hundreds of millions of dollars in damages for thousands of innocent investors in other widely-held funds. *See Wodka v Causeway Capital Mgmt., LLC*, 09-cv-02625 (C.D. Cal. Oct. 9, 2009), *appeal pending*, 09-56733 (9th Cir. Nov. 5, 2009); *Seidl v Am. Century Cos , Inc* , No. 08-cv-08857 (S.D.N.Y. Apr. 28, 2009). The rule of decision applied in this case may also affect the rights of investors in other mutual funds in cases that have yet to be filed. *See generally* M. Ritchel, *Wall St Bets on Gambling on the Web*, N.Y. Times, Dec. 25, 2005 (the problem of U.S. funds investing in illegal gambling was widespread and merited the attention of Congress with calls for a formal Congressional investigation).

authoritative decision.[4] The plurality and dissenting opinions in *Hemi* express sharply differing views concerning the relevance of the common law concept of foreseeability in RICO cases. The undisputed facts of this case afford an opportunity for the Court to clarify for the lower courts the law of intervening causes in the RICO context.

II. The Writ of Certiorari Should Be Granted to Resolve a Split in the Circuits Regarding Whether the Proximate Cause Enquiry Required by *Holmes* May Be Disregarded in Favor of a Mechanical Test

The Court of Appeals refused to conduct the proximate cause enquiry using *any* of the three factors relied on by the Court in *Holmes*. (5a) Its decision

4. The plurality opinion in *Hemi* is not an authoritative determination for other cases because of "the lack of an agreement by a majority of the Court on the principles of law involved." *United States v Pink*, 315 U.S. 203, 216 (1942), *citing Hertz v. Woodman*, 218 U.S. 205 (1910); *see Marks v. United States*, 430 U.S. 188, 193-94 (1977). Justices Breyer, Stevens, and Kennedy expressly disagreed with the plurality view and dissented. The dissenting Justices argued that the "directness" requirement *expands* RICO liability *beyond* what is foreseeable. 130 S. Ct. at 998 (Breyer, *J., dissenting*). Justice Ginsburg concurred with the result but expressly refused to subscribe to the plurality's proximate cause analysis and voted to reverse the case on other grounds. Justice Sotomayor did not participate. She had been a member of the panel that had decided the case in the Court of Appeals. As Petitioners explain in Section III below, the reasoning of the plurality in *Hemi* would not require the dismissal of Petitioners' complaint because Petitioners complain of a direct "first step" injury.

therefore conflicts with the decisions of the Court and other Courts of Appeals on the same important matter. Sup. Ct. Rule 10(a), (c).

Under *Holmes*, questions of RICO proximate causation are resolved by weighing three factors:

i. Whether it will be difficult to ascertain the amount of plaintiff's damages attributable to defendant's wrongful conduct as distinct from other, independent, factors. 503 U.S. at 269.

ii. Whether the court would be forced to adopt complicated rules apportioning damages to obviate the risk of multiple recoveries. *Id.*

iii. Whether there are more directly injured victims who could be counted on to vindicate the law as private attorneys general. *Id.* at 269-70.

In *Holmes*, the defendant manipulated the stock prices of various companies. Certain broker-dealers purchased shares in the companies with their own funds. When the stock manipulation was uncovered, the share prices dropped. This caused the broker-dealers to incur huge losses. These losses then rendered the broker-dealers insolvent and unable to meet their obligations to certain of their customers. The plaintiff in *Holmes*, the Securities Investor Protection Corporation ("SIPC"), was forced to advance nearly $13 million to cover the claims of the customers of the insolvent broker-

dealers. SIPC then sued the stock manipulators under RICO to recover the amounts that it paid to the broker-dealers' customers.

The Court held that the second-hand injuries suffered by SIPC and the customers of the insolvent broker-dealers (*i.e.*, the non-payment of obligations having nothing whatsoever to do with the stock manipulation) were too remote to support a claim by SIPC under RICO. Such "second step" injuries generally are considered too indirect to support proximate causation because – in contrast to the "first step" injuries suffered by the mutual funds here – they flow "merely from the misfortunes visited upon a third person by the defendant's acts." *Id.*, 503 U.S. at 268.[5]

In *Holmes*, the Court said all three factors weighed *against* a finding of proximate cause. In the present case, the Court of Appeals accepted in reaching its decision that all three factors cut *in favor* of a finding of proximate cause (as, in fact, they do). The Court of Appeals, however, refused to rely on those factors, dismissing them as nothing more than the "underlying premises" of the proximate cause requirement. (5a)

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5. The *Holmes* Court noted that a liquidating trustee, suing on behalf of the defunct broker-dealers, would have been a proper plaintiff to seek redress for the manipulation. 503 U.S. at 273. In this derivative action, Petitioners stand in the shoes of the mutual funds for purposes of the proximate cause inquiry, just as a liquidating trustee would have stood in the shoes of the broker-dealers in *Holmes*.

Contrary to the decision of the Court of Appeals, the *Holmes* factors are more than just the underlying premises of the proximate cause requirement. Since *Holmes*, the Court and the lower courts have relied on the *Holmes* factors to guide the requisite proximate cause enquiry.[6] For example, in *Bridge*, the Court determined, by weighing all three *Holmes* factors, that the defendants' racketeering proximately caused the plaintiffs' injuries even though contributing causes had intervened.

Other Circuits agree that proximate causation under RICO ought to be determined on a case-by-case basis using the *Holmes* factors. For example, in *Newcal Indus., Inc. v. IKON Office Solution*, 513 F.3d 1038 (9th Cir. 2008), the district court dismissed RICO claims on grounds other than the *Holmes* factors. The Ninth Circuit reversed and remanded for the trial court to determine proximate causation under the *Holmes* factors. *Id.* at 1055. *Accord, Williams*, 465 F.3d at 1288; *Steamfitters Local Union No. 420 Welfare Fund v. Philip Morris, Inc.*, 171 F.3d 912, 932-34 (3d Cir. 1999).

Petitioners do not contend that the *Holmes* factors represent an exhaustive list of factors to be considered. The Ninth Circuit has described them as a "non-exhaustive" list. *Mendoza v. Zirkle Fruit Co.*, 301 F.3d 1163, 1169 (9th Cir. 2002). One additional factor that is also relevant to the proximate cause enquiry is foreseeability. *See, e.g., Bridge*, 128 S. Ct. at 2144.

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6. The Court has used the same approach in antitrust cases. *See, e.g., Associated Gen. Contractors of Cal., Inc. v. Cal. State Council of Carpenters*, 459 U.S. 519 (1983).

Conversely, not all of the factors will need to be considered in each case. *See, e.g., Hemi*, 130 S. Ct. at 990 (plurality) (discussing only the third *Holmes* factor). Consistent with the Court's precedents, however, the lower courts are not free to disregard all three *Holmes* factors. Nor may they substitute their own alternative tests, particularly when all three *Holmes* factors weigh in favor of finding that proximate cause exists.

The Court of Appeals assumed *arguendo* that all three *Holmes* factors weigh in Plaintiffs' favor and that Petitioners' injuries were reasonably foreseeable. (5a) That being the case, Petitioners' well-pleaded and factually well-supported allegations of proximate cause should have been accepted as true on a motion to dismiss pursuant to Fed. R. Civ. P. 12(b)(6). *Leatherman v. Tarrant County Narcotics Intelligence and Coordination Unit*, 507 U.S. 163, 164 (1993).

Instead of relying on any *Holmes* factor – or any other factor ever relied on by the Court – the Court of Appeals based its decision on a misapplication of a rule based on *In re Am. Express Co. S'holder Litig.*, 39 F.3d 395, 400 (2d Cir. 1994). The Court of Appeals interpreted *American Express* as establishing a black letter rule that "proximate causation is lacking under RICO when the harm results from the exposure or disclosure of the RICO predicate activity." (4a)

The *Holmes* Court cautioned that, in the RICO context (as in the antitrust context), "the infinite variety of claims that may arise make it virtually impossible to announce a black letter rule that will dictate the result

in every case." 503 U.S. at 272 n.20, *quoting Associated Gen. Contractors of Cal., Inc. v. Cal. State Council of Carpenters*, 459 U.S. 519, 536 (1983). The Court repeated that warning in *Bridge*, emphasizing that proximate cause "is a flexible concept that does not lend itself to 'a black-letter rule that will dictate the result in every case.'" 128 S. Ct. at 2142, *quoting Holmes*, 503 U.S. at 272.

The decision of the Second Circuit suffers from the error that the Court has repeatedly warned against. It applied a mechanical test entirely detached from the considerations associated with the proximate cause analysis required by *Holmes*. *See Anza*, 547 U.S. at 460 (the Second Circuit's alternative "rationale does not accord with *Holmes*").

In *American Express*, shareholders of American Express brought a RICO action against the company's officers and directors for a decline in the price of the company's stock. The decline followed the exposure of a secret scheme by American Express officers to defame a competitor in violation of RICO. The exposure of the defendants' racketeering scheme allegedly harmed the *reputation* of American Express and led to the market's loss of faith in the company's leadership. That purportedly resulted in a decrease in the value of the shares of American Express, which injured the plaintiff shareholders. The Court of Appeals found no proximate cause, saying "the commission of the RICO violations was not what injured American Express. Rather, it was the exposure of those acts that caused the appellants' harm." 39 F.3d at 400.

The result in *American Express* can be reached based on a straightforward application of the three *Holmes* factors. For example, the plaintiffs' theory of injury in *American Express* faced daunting attribution issues crucial in weighing the first *Holmes* factor, 503 U.S. at 269. In contrast, Petitioners' investment losses here are not the collateral results of damaged *reputation* from negative publicity. They are the direct result of the loss of the gambling companies' enterprise value when law enforcement shut down their primary source of illegal revenue.

Unfortunately, the *American Express* court's reference to "exposure" has come to be regarded in the Second Circuit as a black letter rule of law that requires the dismissal of any RICO claim where the injury occurs after a previously secret RICO scheme is exposed, even if (as the Court of Appeals assumed for the purpose of deciding this case) the exposure was merely a foreseeable contributing cause.

Furthermore, the ill-defined and mechanical rule for which *American Express* has come to stand – that RICO proximate causation is always lacking when injury results from the "exposure" or "disclosure" of RICO predicate activity – simply has no application to the facts of this case. Here, the harm was not caused by any "exposure" or "disclosure" of Defendants' racketeering activity (*i.e.*, investing in illegal gambling companies). Petitioners do *not* claim that the gambling companies' stock plummeted because of (or had anything to do with) the "exposure" or "disclosure" of Respondents' investments. The fact of Respondents' investments was not secret; it had been reported in their SEC filings.

The intervening cause of the mutual funds' injuries, as identified by the courts below, was *not* the "exposure" or "disclosure" of *any* illegal activity. According to the courts below, the investment losses were caused not by "exposure" of Respondents' illegal acts but by *law enforcement* against the illegal gambling businesses, which (as predicted in the prospectus of one of the gambling companies) caused the mutual funds to lose "a very substantial part of their investment."

This case therefore is a good example of how courts are led into error when they try to resolve proximate cause issues using mechanical tests contrary to the flexible enquiry required by *Holmes*. The Court should grant certiorari to resolve a split in the Circuits regarding the significance of the *Holmes* factors.

III. The Writ of Certiorari Should Be Granted to Resolve Whether a Plaintiff Who Suffers a Direct RICO Injury Must Satisfy a Stricter Standard of Proximate Cause Than that Required Under the Common Law

Petitioners allege a "first step" RICO injury suffered directly by the mutual funds that is neither contingent on the harm suffered by third parties nor "entirely distinct" from the RICO violations. Nevertheless, the Court of Appeals required Petitioners to satisfy a stricter standard of proximate cause than that required by the common law. In rejecting the application of common law "foreseeability" principles to Petitioners' "first step" RICO injuries, the Court of Appeals decided an important question of federal law contrary to decisions of the Court. Sup. Ct. Rule 10(c). In addition,

the decision of the Court of Appeals conflicts with the decisions of other Courts of Appeals on the same important matter. Sup. Ct. Rule 10(a).

Petitioners submit that RICO proximate cause for a "first step" injury imposes no greater burden on a plaintiff than the common law requirement. Other Circuits have interpreted *Holmes* as mandating the application of common law proximate cause principles – which focus on foreseeability – to cases alleging "first step" RICO injuries. *See RWB Servs., LLC v. Hartford Computer Group, Inc.*, 539 F.3d 681, 688 (7th Cir. 2008); *Trollinger v. Tyson Foods, Inc.*, 370 F.3d 602, 615 (6th Cir. 2004) (a "first step" RICO injury must satisfy the "traditional requirements of proximate cause – that the wrongful conduct be a substantial and foreseeable cause and that the connection be logical and not speculative"); *Mid Atlantic Telecom*, 18 F.3d at 263 (4th Cir. 1994); *Cox*, 17 F.3d at 1399 (11th Cir. 1994) (applying common law principles to RICO proximate cause determination).

Issuance of a writ of certiorari in this case is particularly appropriate in light of the Court's most recent effort to clarify the law in this area. In *Hemi*, 130 S. Ct. 983, a plurality of the Court held that where the plaintiff's injury is purely contingent on the harm to a *third* party caused by a *fourth* party, *see id.* at 990, such a theory of causation moves "well beyond the first step" and cannot meet RICO's requirement for "direct" injury regardless of whether it was foreseeable. *Id.* at 989.

The facts of *Hemi* were critical to the plurality's decision. Hemi was a New Mexico company that sold cigarettes over the Internet to New York City residents.

Such sales were subject to taxes by both the State of New York and the City. Hemi failed to file certain reports with the State pursuant to the Jenkins Act, which required out-of-state vendors such as Hemi to disclose customer information to the states into which they shipped cigarettes. Pursuant to an agreement between the State and the City, the State was obligated to pass customer information it received from Jenkins Act reports to the City so that the City could collect taxes directly from City residents. The City alleged that Hemi's failure to file the required Jenkins Act reports with the State constituted RICO predicate crimes of mail and wire fraud. According to the City, Hemi's racketeering activity not only deprived the State of its ability to collect state taxes on cigarette sales to New York, it also caused the City to lose taxes owed by City residents. The City argued that because the State was unable to pass along Hemi's customer information to the City, the City was deprived of the ability to collect taxes directly from the City's residents. Based on these facts, the *Hemi* plurality declined to

> extend RICO liability to situations where the defendant's fraud on the third party (the State) has made it easier for a *fourth* party (the taxpayer) to cause harm to the plaintiff (the City). Indeed, the fourth-party taxpayers here only caused harm to the City in the first place if they decided not to pay taxes they were legally obligated to pay.

130 S. Ct. at 990.

In reaching its decision, the *Hemi* plurality relied extensively on *Anza*. In that case, a merchant sued its competitor under RICO alleging that it was injured because the competitor failed to charge sales tax and submitted fraudulent tax returns to the State of New York. The competitor was thus able to undercut the plaintiff's price. In finding that the plaintiff had failed to allege proximate causation, the Court explained that "[t]he cause of [the plaintiff's] asserted harms . . . is a set of actions (offering lower prices) *entirely distinct* from the alleged RICO violation (defrauding the State)." *Id.* at 458 (emphasis added). The alleged RICO violation directly caused the State to be defrauded of taxes, not the plaintiff to lose money to its competitor. *Id.*

Unlike in *Hemi* and *Holmes*, Petitioners here do not complain of second-hand injuries "purely contingent" on the harm suffered directly by third parties. *Hemi*, 130 S. Ct. at 989; *Holmes*, 503 U.S. at 271. Instead, Petitioners sue on behalf of "first step" injured parties.[7] There is no party more directly harmed by Respondents' illegal investments than the mutual funds on whose behalf Petitioners sue, and, as accepted by the Court of Appeals (4a), no better situated plaintiff would have an incentive to sue. *See Hemi*, 130 S. Ct. at 990; *Bridge*128 S. Ct. at 2144; *Holmes*, 503 U.S. at 269-70.

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7. The reference to "first step" in *Holmes*, 503 U.S. at 271-272 was based on a quotation from *Associated Gen Contractors*, 459 U.S. at 534, which held that a union could not recover under the antitrust laws for the contingent injury it allegedly suffered by reason of the defendants' coercion directed against third parties. The Sixth Circuit has described these as "passed-on" injuries. *Trollinger*, 370 F.3d at 613-15.

Moreover, unlike in *Hemi* and *Anza*, Petitioners do not complain of injury from causes "entirely distinct" from the underlying racketeering activity. *Hemi*, 130 S. Ct. at 990; *Anza*, 547 U.S. at 458. Rather, government enforcement of the criminal laws could not possibly have caused any harm to the mutual funds had there been no illegal investments "in the first place." *Hemi*, 130 S. Ct. 983. Defendants' predicate crimes therefore were the primary, efficient, and substantial cause of the mutual funds' losses.

The *Holmes* Court relied on "common law" proximate causation within the statutory framework of RICO because of similar language and attendant proximate cause requirements under the antitrust laws. When Congress enacted § 4 of the Clayton Act, § 7 of the Sherman Act read in relevant part: "Any person who shall be injured in his business or property by any other person or corporation by reason of anything forbidden or declared to be unlawful by this act, may sue . . . ." 26 Stat. 210 (1890). Interpreting this language, the Court held that Congress had intended to "incorporate common-law principles of proximate causation." *Holmes*, 503 U.S. at 267, *citing Associated Gen. Contractors*, 459 U.S. at 533-34 & n.29, 536 n.33. The *Holmes* Court therefore concluded that "[w]e may fairly credit the 91st Congress, which enacted RICO, with knowing the interpretation federal courts had given the words earlier Congresses had used first in § 7 of the Sherman Act, and later in the Clayton Act's § 4." 503 U.S. at 268.

The Court has never held that RICO proximate causation for "first step" injuries such as those complained of by Petitioners is any more demanding than

ordinary common law proximate causation. Indeed, the Court explicitly stated in *Holmes* that "our use of the term 'direct' should merely be understood as a reference to the proximate-cause enquiry." *Id.* at 268 & 272 n.20. That enquiry should be guided by the three factors weighed by the Court in *Holmes*, and by other established common law concepts, such as foreseeability, *see Bridge*, 128 S. Ct. at 2144.

Congress expressly provided that the RICO statute is to "be liberally construed to effectuate its remedial purposes," Pub.L. 91-452, § 904(a), 84 Stat. 947 (1970). *See Sedima, S.P.R.L. v. Imrex Co., Inc.*, 473 U.S. 479, 497-98 (1985). There is no basis in the language of RICO or its legislative history, or in the Court's precedents, to impose a more stringent proximate cause requirement than the common law requirement, at least in the case of "first step" injuries. In light of the express Congressional admonition that RICO is to be liberally construed, "[c]ourts should not erect artificial barriers – metaphysical or otherwise – as a means of keeping RICO cases off the federal dockets." *Sun Savings and Loan Ass'n v. Dierdorff*, 825 F.2d 187, 194 (9th Cir. 1987).

The Second Circuit's aberrant and unduly restrictive construction of RICO is contrary to the statutory mandate, the Court's precedents, and the decisions of other Courts of Appeals. Certiorari should be granted to decide the important question whether a plaintiff alleging a "first step" RICO injury must satisfy a stricter standard of proximate cause than that required at common law.

Furthermore, in *Hemi*, the plurality held that principles of foreseeability do not govern RICO proximate cause in the context of injuries that go beyond the "first step." In doing so, however, the plurality broadly suggested that foreseeability may *never* be relevant to RICO proximate cause analysis. *Hemi*, 130 S. Ct. 991 ("[o]ur precedents make clear that in the RICO context, the focus is on the directness of the relationship between the conduct and the harm. Indeed, *Anza* and *Holmes* never even mention the concept of foreseeability"). *But see Bridge*, 128 S. Ct. at 2144 ("foreseeable and natural" consequences of racketeering satisfy proximate causation under RICO). In light of this, it is particularly urgent for the Court to provide authoritative guidance, lest *Hemi* expand beyond "the limit of its logic." B. Cardozo, *The Nature of the Judicial Process* 51 (1921). If left unclarified, the uncertainty regarding whether foreseeability is ever relevant, even in "first step" RICO cases like this one, will sow confusion among the lower courts and lead to more decisions, such as the one below, announcing unwarranted departures from fundamental principles of proximate causation.

CONCLUSION

For all the foregoing reasons, Petitioners respectfully request that the Supreme Court grant review of this matter.

Respectfully submitted,

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APPENDIX A — SUMMARY ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT DATED AND FILED NOVEMBER 23, 2009

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

No. 09-1445-cv

DEANNA MCBREARTY, MARYLYNN HARTSEL, individually, derivatively, and on behalf of all others similarly situated,

Plaintiffs-Appellants,

-v.-

THE VANGUARD GROUP, INC., GEORGE U. SAUTER, DUANE F. KELLY, JOHN J. BRENNAN, CHARLES D. ELLIS, RAJIV L. GUPTA, AMY GUTMANN, JOANN HEFFERNAN HEISEN, ANDRE F. PEROLD, ALFRED M. RANKIN JR., J. LAWRENCE WILSON, ACADIAN ASSET MANAGEMENT, LLC, RONALD D. FRASHURE, JOHN R. CHISHOLM, BRIAN K. WOLAHAN, MARATHON ASSET MANAGEMENT, LLP and NEIL M. OSTRER,

Defendants-Appellees,

Appendix A

VANGUARD INTERNATIONAL EQUITY INDEX FUNDS, D/B/A VANGUARD EUROPEAN STOCK INDEX FUND, VANGUARD HORIZON FUNDS, D/B/A VANGUARD GLOBAL EQUITY FUND,

Nominal Defendants-Appellees,

ALLIANCE BERNSTEIN LP, HENRY S. D'AURIA, SHARON E. FAY, KEVIN F. SIMMS, WILLIAM J. ARAH and JEREMY H. HOSKING,

Defendants.

November 20, 2009, Decided

PRESENT:

HON. RALPH K. WINTER,
HON. ROSEMARY S. POOLER,
Circuit Judges,
HON. JED S. RAKOFF,
*District Judge.**

SUMMARY ORDER

UPON DUE CONSIDERATION, IT IS HEREBY ORDERED, ADJUDGED, AND DECREED that the judgment of the district court is **AFFIRMED.**

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* The Honorable Jed S. Rakoff, United States District Judge for the Southern District of New York, sitting by designation.

Appendix A

Plaintiffs-appellants appeal a judgment entered on April 6, 2009 in the United States District Court for the Southern District of New York (Cote, *J.*) dismissing with prejudice plaintiffs' claims under the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961 *et seq.* ("RICO"). Plaintiffs were shareholders in certain of defendants' mutual funds that had invested in online gambling companies. They brought this civil RICO action after the shares of these online gambling companies declined in value following a government crackdown on illegal offshore gambling. We assume general familiarity with the underlying facts, procedural history, and issues on appeal.

We review *de novo* the district court's grant of a motion to dismiss, taking all reasonable inferences in plaintiffs' favor. *City of N.Y. v. Smokes-Spirits.com, Inc.*, 541 F.3d 425, 439 (2d Cir. 2008).

To state a civil RICO claim, plaintiffs must show that they were injured "by reason of" the alleged racketeering activity, 18 U.S.C. § 1964(c), that is, that the defendant's RICO violation proximately caused plaintiffs' injuries. *See Anza v. Ideal Steel Supply Corp.*, 547 U.S. 451, 457, 126 S. Ct. 1991, 164 L. Ed. 2d 720 (2006); *Holmes v. Sec. Investor Prot. Corp.*, 503 U.S. 258, 267-68, 112 S. Ct. 1311, 117 L. Ed. 2d 532 (1992); *see also Smokes-Spirits*, 541 F.3d at 440-41; *Lerner v. Fleet Bank, N.A.*, 318 F.3d 113, 121-22 (2d Cir. 2003). In the RICO context, proximate causation means, in turn, that "the alleged violation led directly to the plaintiff's injuries." *Anza*, 547 U.S. at 461. Here, however, the

complaint alleges that the decline in the funds' online gambling holdings was not the direct result of the RICO violation —the owning and/or financing of illegal gambling — but rather was the result of the subsequent "government crackdown" on the illegal gambling. Although plaintiffs contend that the law enforcement crackdown was a foreseeable risk of defendants' activities (rather than a supervening cause),[1] we have already held that proximate causation is lacking under RICO when the harm results from the exposure or disclosure of the RICO predicate activity. *In re Am. Express Co. S'holder Litig.*, 39 F.3d 395, 400 (2d Cir. 1994).[2]

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1. Although foreseeability is often the test of proximate causation at common law, *see Palsgraf v. Long Island R.R. Co.*, 248 N.Y. 339, 162 N.E. 99, 100 (N.Y. 1928), RICO causation is a concept distinct from "proximate causation as that term is used at common law." *Abrahams v. Young & Rubicam Inc.*, 79 F.3d 234, 237 (2d Cir. 1996).

2. Although plaintiffs argue that *American Express* is undercut by the Supreme Court's recent decision in *Bridge v. Phoenix Bond & Indemnity Co.*, 128 S. Ct. 2131, 170 L. Ed. 2d 1012 (2008), we do not agree. The civil RICO action in *Bridge* was brought by regular bidders at a county's auctions of tax liens, who alleged that the defendants, also regular bidders, were able to obtain a disproportionate share of valuable liens by lying to the county about their status as "related entities" in order to circumvent a rule that would otherwise result in a more equitable distribution of liens. *Id* at 2135-36. Thus, the injury alleged in *Bridge* — the plaintiffs' inability to obtain valuable liens to which they would otherwise have been entitled — resulted directly from the fraudulent representations that constituted the racketeering activity.

Plaintiffs also argue that the "underlying premises" of the proximate cause requirement set forth by the Supreme Court in *Holmes v. Securities Investor Protection Corp.*, 503 U.S. at 269-70, support a finding of proximate cause here.[3] It is hardly clear that this is so; but even assuming *arguendo* that these policy considerations cut in plaintiffs' favor, they cannot remedy the basic defects in causation discussed above, nor provide a basis for overruling our clear prior precedents.

For the foregoing reasons, the judgment of the district court is hereby **AFFIRMED**.

FOR THE COURT:
Catherine O'Hagan Wolfe, Clerk

BY: Frank Perez

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3. These considerations are: "(1) the factual difficulty of measuring indirect damages and distinguishing among distinct independent causal factors; (2) the complexity of apportioning damages among plaintiffs 'to obviate the risk of multiple recoveries'; and (3) the fact that 'the need to grapple with these problems is simply unjustified by the general interest in deterring injurious conduct, since directly injured victims can generally be counted on to vindicate the law.'" *Smokes-Spirits*, 541 F.3d at 440 (quoting *Holmes*, 503 U.S. at 269).

APPENDIX B — OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK DATED AND FILED APRIL 2, 2009

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

08 Civ. 7650 (DLC)

DEANNA McBREARTY and MARYLYNN HARTSEL, individually, derivatively and on behalf of all others similarly situated,

Plaintiffs,

-v-

THE VANGUARD GROUP, INC.; GEORGE U. SAUTER; DUANE F. KELLY; JOHN J. BRENNAN; CHARLES D. ELLIS; RAJIV L. GUPTA; AMY GUTMANN; JOANN HEFFERNAN HEISEN; ANDRE F. PEROLD; ALFRED M. RANKIN, JR.; J. LAWRENCE WILSON; ACADIAN ASSET MANAGEMENT, LLC; RONALD D. FRASHURE; JOHN R. CHISHOLM; BRIAN K. WOLAHAN;; ALLIANCEBERNSTEIN LP; HENRY S. D'AURIA; SHARON E. FAY; KEVIN F. SIMMS; MARATHON ASSET MANAGEMENT LLP; WILLIAM J. ARAH; JEREMY H. HOSKING; and NEIL M. OSTRER,

Defendants,

-and-

Appendix B

VANGUARD INTERNATIONAL EQUITY INDEX FUNDS, d/b/a VANGUARD EUROPEAN STOCK INDEX FUND; and VANGUARD HORIZON FUNDS, d/b/a VANGUARD GLOBAL EQUITY FUND,

Nominal Defendants.

April 2, 2009, Decided
April 2, 2009, Filed

DENISE COTE, District Judge:

This lawsuit concerns an investment fund's liability to its shareholders for investments in online gambling companies. The investments declined in value after the gambling companies became the targets of a United States government crackdown. Plaintiffs, each a shareholder in one of the nominal defendants, bring this derivative and putative class action lawsuit alleging violations of the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961-1968 ("RICO"), as well as state-law claims for breach of fiduciary duty, negligence and waste. Defendants have moved to dismiss the complaint arguing that, *inter alia*, plaintiffs lack statutory standing under RICO because they cannot show that they were injured "by reason of" the defendants' alleged RICO violations. Plaintiffs having been injured by the government's enforcement actions and their attendant publicity, and only indirectly (at best) by the defendants' purchase of stock, their RICO claims are dismissed for failure to plead proximate causation.

Appendix B

BACKGROUND

The following facts are taken from the complaint. Plaintiff Deanna McBrearty purchased shares in nominal defendant Vanguard European Stock Index Fund ("Vanguard European") on or about May 20, 2005. Plaintiff Marylynn Hartsel purchased shares in nominal defendant Vanguard Global Equity Fund ("Vanguard Global") sometime prior to July 1, 2006.[1] Plaintiffs allege that the nominal defendants repeatedly purchased shares in "illegal gambling businesses," as defined by 18 U.S.C. § 1955. In or about 2006, federal and state law enforcement agencies "began a crackdown" on gambling businesses, such as those in which the nominal defendants had invested. Consequently, the stock prices of the gambling business owned by the nominal defendants dropped precipitously, and plaintiffs' portfolios declined in value. The plaintiffs name as defendants the investment advisor and the portfolio managers responsible for investment decisions made by the nominal defendants and individuals associated with each of these entities.

Plaintiffs allege that, by purchasing and holding stock in the gambling businesses subject to the government's enforcement activities, the defendants conspired together to commit predicate acts under RICO by "finane[ing]" or "own[ing]" an illegal gambling business, in violation of 18 U.S.C. § 1955. Their

1. Vanguard European and Vanguard Global will be referred to collectively as the "nominal defendants."

investments in gambling businesses over a multi-year period, plaintiffs assert, constitute a pattern of racketeering activity that injured plantiffs "as a direct and proximate result."

This action was filed on August 29, 2008. On October 27, 2008, the defendants moved to dismiss the complaint. Plaintiffs' opposition, filed on November 24, asserted that their complaint was sufficient to withstand defendants' motions, but requested leave to amend in the alternative.

At a December 18 conference, the parties agreed with the Court's proposal to initially address two of the issues raised in the motions to dismiss — whether plaintiffs had demonstrated that defendants' alleged RICO violations caused their injuries, thereby conferring standing to sue under RICO, and the sufficiency of the purchase of gambling-company stock as a predicate act under RICO. A finding in the defendants' favor on either issue, the parties agreed, could not be cured by amendment. Were the plaintiffs to prevail on both issues, they would then have the opportunity to amend their complaint to cure any possible deficiencies, and then the remainder of defendants' motions to dismiss would be considered. As explained below, it is only necessary to reach the first of these two issues to conclude that the RICO claim must be dismissed.

Appendix B

DISCUSSION

A trial court considering a Rule 12(b)(6) motion must "accept as true all factual statements alleged in the complaint and draw all reasonable inferences in favor of the non-moving party." *McCarthy v. Dun & Bradstreet Corp.*, 482 F.3d 184, 191 (2d Cir. 2007). At the same time, "conclusory allegations or legal conclusions masquerading as factual conclusions will not suffice to defeat a motion to dismiss." *Achtman v. Kirby, McInerney & Squire, LLP*, 464 F.3d 328, 337 (2d Cir. 2006) (citation omitted). A court considering a Rule 12(b)(6) motion applies a "flexible plausibility standard, which obliges a pleader to amplify a claim with some factual allegations in those contexts where such amplification is needed to render the claim plausible." *Boykin v. KeyCorp*, 521 F.3d 202, 213 (2d Cir. 2008) (citation omitted). "To survive dismissal, the plaintiff must provide the grounds upon which his claim rests through factual allegations sufficient to raise a right to relief above the speculative level." *ATSI Commc'ns, Inc. v. Shaar Fund, Ltd.*, 493 F.3d 87, 98 (2d Cir. 2007).

Defendants assert that plaintiffs cannot plausibly allege a violation of RICO, because they cannot plead that defendants' alleged violations of RICO proximately caused plaintiffs' injuries. RICO's civil provision, 18 U.S.C. § 1964(c), provides a private cause of action for any person injured in her business or property "by reason of" a violation of RICO. *McLaughlin v. American Tobacco Co.*, 522 F.3d 215, 222 (2d Cir. 2008) (citing 18 U.S.C. § 1964(c)). In *Holmes v. Securities*

Appendix B

Investor Protection Corporation, 503 U.S. 258, 112 S. Ct. 1311, 117 L. Ed. 2d 532 (1992), the Supreme Court refined its earlier conception of causation (the "by reason of" requirement) and explicitly imposed a proximate causation requirement for civil RICO actions. Three policy considerations informed its decision to limit the plaintiffs who could recover from a RICO violation to those who were directly or proximately injured:

> (1) the factual difficulty of measuring indirect damages and distinguishing among distinct independent causal factors;
>
> (2) the complexity of apportioning damages among plaintiffs to obviate the risk of multiple recoveries; and
>
> (3) the fact that the need to grapple with these problems is simply unjustified by the general interest in deterring injurious conduct, since directly injured victims can generally be counted on to vindicate the law.

Smokes-Spirits.Com, Inc., 541 F.3d at 440 (citing *Holmes*, 503 U.S. at 269). Thus, "[t]o fulfill the requirement that the injury occur 'by reason of a defendant's action, a plaintiff must show that the defendant's violation not only was a 'but for' cause of his injury, but was the proximate cause as well." *McLaughlin*, 522 F.3d at 222 (citation omitted).

Proximate causation, or loss causation, does not exist where the plaintiff's injury was "indirectly (and hence not proximately) caused by the racketeering activity." *Baisch v. Gallina*, 346 F.3d 366, 373 (2d Cir. 2003). *See also Anza v. Ideal Steel Supply Corp.*, 547 U.S. 451, 460, 126 S. Ct. 1991, 164 L. Ed. 2d 720 (2006) (proximate cause requires a "direct causal connection" between the RICO violations and the injury suffered). Injuries that are "too attenuated" from the RICO predicate acts are too remote to satisfy the proximate cause requirement. *City of New York v. Smokes-Spirits.Com, Inc.*, 541 F.3d 425, 440 n.20 (2d Cir. 2008). Proximate cause is thus lacking where the cause of the asserted harms is "a set of actions . . . entirely distinct from the alleged RICO violation." *Id.* at 441 (citation omitted). "[W]hen factors other than the defendant's [misconduct] are an intervening direct cause of a plaintiff's injury, that same injury cannot be said to have occurred by reason of the defendant's actions." *McLaughlin*, 522 F.3d at 226 (citation omitted). Injuries occurring because of the disclosure of a scheme involving the predicate acts, rather than because of the predicate acts themselves, are not the "necessary result" of the predicate acts, and do not give rise to RICO standing. *In re Am. Express Co. Shareholder Litig.*, 39 F.3d 395, 400 (2d Cir. 1994) (citation omitted). *See also Abrahams v. Young & Rubicam Inc.*, 79 F.3d 234, 239 (2d Cir. 1996).

Put otherwise, a defendant accused of violating RICO is potentially liable only "to those with respect to whom his acts were a substantial factor in the sequence of responsible causation, and whose injury was

reasonably foreseeable or anticipated as a natural consequence." *Baisch*, 346 F.3d at 373-74 (citation omitted). Those whose injuries are "reasonably foreseeable or anticipated as a natural consequence" generally include "the targets, competitors, and intended victims of the racketeering enterprise." *Lerner v. Fleet Bank, N.A.*, 318 F.3d 113, 124 (2d Cir. 2003).[2]

Proximate causation is lacking here because the shareholders were injured not by the ownership of or investment in the illegal gambling operations, but by the reaction of the stock price to the publicity following the government's investigation of those operations. "[T]he commission of the RICO violations was not what injured" plaintiffs; as they acknowledge, "it was the exposure of those acts," through the government's investigation, as illegal that "caused the [plaintiffs'] harm." *American Express*, 39 F.3d at 400. The direct cause of plaintiffs' injuries is therefore a "set of actions [the government crackdown] entirely distinct from the alleged RICO violation [conducting an illegal gambling operation]." *Smokes-Spirits*, 541 F.3d at 441 (citation omitted). An injury created by the disclosure of a scheme or, similarly, by intervening actions (the government investigation), does not give rise to RICO standing. *American Express*, 39 F.3d at 400.

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2. The relationship between the zone of interests analysis and more recent formulations of proximate cause is discussed in *Smokes-Spirits*, 541 F.3d at 440 n.20.

Further, as in *American Express*, "the shareholders . . . were certainly not the intended targets of the RICO violations," but were the intended beneficiaries of the investments in the gambling funds. *Id.* Plaintiffs' protestations that proximate causation does not require that their injury be the "preconceived purpose" or "specifically intended consequence" of the predicate acts does not displace the forseeability requirement, which under *Lerner* is generally limited to injuries incurred by "targets, competitors, and intended victims" of the RICO violations. *Lerner*, 318 F.3d at 124.

Plaintiffs have raised no plausible claim that they are a member of any of these groups. Those who lost money by gambling online, or competitors offering legal gambling services are the ones who may be able to argue that they are the reasonably foreseeable intended victims, competitors, or targets of illegal gambling operations. Indeed, cases from this Circuit and elsewhere, when discussing victims of gambling enterprises, refer to those who gambled and lost, and not to investors in the enterprise. *See, e.g.*, *Price v. Pinnacle Brands, Inc.*, 138 F.3d 602, 607 (5th Cir. 1998); *United States v. Joseph*, 835 F.2d 1149, 1152 (6th Cir. 1987); *United States v. Littman*, 421 F.2d 981, 982 (2d Cir. 1970). Plaintiffs, as those providing economic backing for the gambling investments, were not the intended victims or targets of this enterprise.

Plaintiffs rely instead on the three policy considerations identified in *Holmes* and subsequently cited by the Second Circuit in *Smokes-Spirits*, which underlie the adoption of the proximate cause test. *Holmes*, 503 U.S. at 269; *Smokes-Spirits*, 541 F.3d at 440. They attempt to argue that they

are the parties best situated to bring RICO claims to recover on the shareholders' behalf. Plaintiffs argument misses the point; the *Holmes* factors support but do not alter the analysis of proximate causation discussed above. Because intervening events, and not the defendants' investment decisions, proximately caused the plaintiffs' investment losses, plaintiffs' RICO claims must be dismissed for lack of causation.

CONCLUSION

Plaintiffs' RICO claims are dismissed with prejudice. As there are no longer any federal claims against the defendants in this suit, it is within the Court's discretion whether to exercise supplemental jurisdiction over plaintiffs' state law claims. *Klein & Co. Futures, Inc. v. Board of Trade of City of New York*, 464 F.3d 255, 263 (2d Cir. 2006). Since this action has not yet proceeded to the merits of plaintiffs' claims, this Court declines to exercise supplemental jurisdiction. The Clerk of Court shall enter judgment for the defendants on the RICO claim and dismiss the remaining claims without prejudice to refiling in state court.

SO ORDERED:

Dated: New York, New York
April 2, 2009

s/ Denise Cote
DENISE COTE
United States District Judge

APPENDIX C — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT DENYING PETITION FOR REHEARING DATED AND FILED JANUARY 12, 2010

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse, 500 Pearl Street, in the City of New York, on the 12th day of January, two thousand ten.

No. 09-1445-cv

DEANNA MCBREARTY, MARYLYNN HARTSEL, individually, derivatively, and on behalf of all others similarly situated,

Plaintiffs-Appellants,

-v.-

THE VANGUARD GROUP, INC., GEORGE U. SAUTER, DUANE F. KELLY, JOHN J. BRENNAN, CHARLES D. ELLIS, RAJIV L. GUPTA, AMY GUTMANN, JOANN HEFFERNAN HEISEN, ANDRE F. PEROLD, ALFRED M. RANKIN JR., J. LAWRENCE WILSON, ACADIAN ASSET MANAGEMENT, LLC, RONALD D. FRASHURE, JOHN R. CHISHOLM, BRIAN K. WOLAHAN, MARATHON ASSET MANAGEMENT, LLP and NEIL M. OSTRER,

Defendants-Appellees,

Appendix C

VANGUARD INTERNATIONAL EQUITY INDEX FUNDS, D/B/A VANGUARD EUROPEAN STOCK INDEX FUND, VANGUARD HORIZON FUNDS, D/B/A VANGUARD GLOBAL EQUITY FUND,

Nominal Defendants-Appellees,

ALLIANCE BERNSTEIN LP, HENRY S. D'AURIA, SHARON E. FAY, KEVIN F. SIMMS, WILLIAM J. ARAN and JEREMY H. HOSKING,

Defendants.

Deanna McBrearty and Marylynn Hansel having filed a petition for panel rehearing, or, in the alternative, for rehearing *en banc*, and the panel that determined the appeal having considered the request for panel rehearing, and the active members of the Court having considered the request for rehearing *en banc*,

IT IS HEREBY ORDERED that the petition is denied.

FOR THE COURT:
Catherine O'Hagan Wolfe, Clerk

By: s/ Frank Perez
Frank Perez, Deputy Clerk

No. 09-1187

SUPREME COURT, U.S.
FILED
MAY 3 2010

IN THE

Supreme Court of the United States

DEANNA MCBREARTY, *et al.*,
Petitioners,

v.

THE VANGUARD GROUP, INC., *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF FOR RESPONDENTS IN OPPOSITION

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May 3, 2010

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QUESTION PRESENTED

Whether a complaint brought by investors in a mutual fund alleging that the fund invested in publicly traded companies whose stock prices then fell after the government prosecuted them as illegal gambling businesses is properly dismissed for failure to allege proximate causation under the Racketeer Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. § 1964(c), because, even if the mutual fund's supposed "ownership" or "financing" of illegal gambling businesses were a predicate act, the fall in stock prices was not alleged to be "by reason of" the mutual fund's investments.

CORPORATE DISCLOSURE STATEMENT

Pursuant to Supreme Court Rule 29.6, Respondents state as follows:

1. Respondent The Vanguard Group, Inc. has no parent corporation, and no publicly held company owns 10% or more of its stock.

2. Respondent Acadian Asset Management, LLC ("Acadian") has a parent corporation, Old Mutual Asset Managers (US) LLC, which owns 100% of Acadian's Class A shares (*i.e.*, voting shares) and at least 71.43% of Acadian's Class B shares. Old Mutual Asset Managers (US) LLC is a wholly owned subsidiary of Old Mutual (US) Holdings, Inc., which is a wholly owned subsidiary of OM Group (UK) Limited, which is a wholly owned subsidiary of Old Mutual PLC, which is a publicly traded company. Other than Old Mutual PLC's indirect ownership interest, no publicly held company owns 10% or more of Acadian.

3. Respondent Marathon Asset Management, LLP has no parent corporation, and no publicly held company owns 10% or more of its stock.

4. Respondents Vanguard International Equity Index Fund d/b/a Vanguard European Stock Index Fund and Vanguard Horizon Funds d/b/a Vanguard Global Equity Fund have no parent corporations, and no publicly held companies own 10% or more of their stock.

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IN THE

Supreme Court of the United States

No. 09-1187

DEANNA MCBREARTY, *et al.*,
Petitioners,

v.

THE VANGUARD GROUP, INC., *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF FOR RESPONDENTS IN OPPOSITION

Petitioners attempted below to state claims under RICO to recover alleged investment losses. They claimed that the mutual funds in which they had invested had committed predicate acts by purchasing publicly traded shares of certain online gambling companies, and that a subsequent government "crackdown" on such companies had caused the companies' stock prices to fall, leading in turn to declines in the value of their investments. Without addressing whether the mutual funds' public stock purchases described by Petitioners could qualify as RICO predicate acts, the Second Circuit found that Petitioners had failed to allege they were injured "by reason of" the mutual funds' purchases of stock, as opposed to the "crackdown."

Contrary to Petitioners' assertions, the lower court's dismissal of Petitioners' novel RICO theory for lack of proximate cause is not in conflict with the decisions of this Court or of other circuits. *Bridge v. Phoenix Bond & Indemnity Co.*, 128 S. Ct. 2131 (2008), involved harm to competing bidders when the defendants rigged an auction. It did not involve intervening causes, and its holding is entirely consistent with the decision below. Nor does the Second Circuit's decision not to include in its summary order a detailed analysis of policy considerations discussed in *Holmes v. Securities Investor Protection Corp.*, 503 U.S. 258 (1992), present any conflict with *Holmes*. *Holmes* found that no proximate cause had been alleged where plaintiffs claimed defendants' stock manipulation scheme bankrupted two broker-dealers and forced them to reimburse the broker-dealers' customers; its holding in no way suggests that proximate cause is supported by Petitioners' even more attenuated allegations. With respect to the recent decision in *Hemi Group, LLC v. City of New York*, 130 S. Ct. 983 (2010), not only is there no majority opinion, but the decision below would be affirmed under the reasoning of both the plurality and the dissent. And *Hemi* addressed a claim that failure to report cigarette sales impeded New York City's ability to collect taxes, not any intervening cause such as alleged here. Further, there is no circuit split, for none of the circuit court decisions cited by Petitioners involve investors in a fund that allegedly owned an illegal business or alleged injuries caused by actions of law enforcement.

Respondents respectfully submit that, absent a conflict with decisions of this Court or a circuit split, there is no justification for granting certiorari. This case does not present an issue that is recurring or of

any national importance. It is also a poor vehicle for deciding any RICO proximate cause issue because Respondents have two alternative grounds to support the judgment: the alleged basis for Petitioners' claims, purchases of shares on a public stock exchange, is not a RICO predicate act, and Petitioners and their alleged injuries fall outside the scope of the statute on which they seek to base their RICO suit.

Accordingly, the petition for a writ of certiorari should be denied.

COUNTERSTATEMENT

This case concerns investments made by two Vanguard mutual funds in publicly traded shares of four online gambling companies. Petitioners' complaint alleged that they were investors in the mutual funds, and that Vanguard and its trustees and investment advisors (collectively "Respondents") were liable for declines in the value of the gambling company investments after the U.S. government commenced a "crackdown" on online gambling, causing online gambling companies to withdraw from the U.S. market and their stock prices to drop.

Petitioners identified the gambling companies as Party Gaming PLC, Sportingbet PLC, BWin Interactive Entertainment AG, and NETeller PLC. C.A. App. 134. All four companies are based in Europe and listed on European stock exchanges. C.A. App. 137-52. Petitioners alleged that, "in or about 2006, federal and state law enforcement agencies began a crackdown on illegal gambling businesses . . . . As a result, the stock prices of all such illegal gambling businesses fell substantially." C.A. App. 32. As part of the "crackdown," Congress adopted the Unlawful

Internet Gambling Enforcement Act ("UIGEA"), which prohibited the use of credit cards and wire transfers in connection with certain online gambling. 31 U.S.C. §§ 5361-5367, Pub. L. No. 109-347, Title VIII, 120 Stat. 1952 (Oct. 13, 2006). The New York Times reported that following passage of this legislation on a Friday, shares of some online gambling companies lost "more than half of their value within minutes Monday morning." C.A. App. 278.

Petitioners brought claims, individually and derivatively on behalf of the funds, alleging breach of fiduciary duty, negligence, and waste. In addition to these conventional state-law claims, they also asserted a novel RICO claim based on 18 U.S.C. § 1955, which criminalizes the financing, management, supervision, direction, or ownership of gambling businesses that violate state law. Petitioners theorized that public minority shareholders were guilty of a felony under Section 1955, and this could qualify as a RICO predicate act. Petitioners alleged that the funds had committed crimes by purchasing shares in the public gambling companies, and that Respondents had engaged in a pattern of racketeering activity by causing the funds to so invest.

Respondents filed motions to dismiss on a number of grounds, including failure to plead RICO proximate cause and failure to plead cognizable predicate acts. The district court addressed these RICO issues first, because Petitioners conceded that they would not be able to improve their RICO allegations with amendment. Pet. App. 9a. After considering these issues, the district court dismissed the complaint, finding that "[p]roximate causation is lacking here because the shareholders were injured not by the ownership of or investment in the illegal gambling

operations, but by the reaction of the stock price to the publicity following the government's investigation of those operations." Pet. App. 13a.

In reaching this conclusion, the district court cited a prior decision of the Second Circuit that had affirmed the dismissal of a similarly attenuated RICO claim. Pet. App. 13a-14a (citing *In re American Express Shareholder Litig.*, 39 F.3d 395 (2d Cir. 1994)). In *American Express*, shareholders had asserted RICO claims against American Express on the ground that the company had engaged in mail and wire fraud in defaming a competitor and that its stock price had declined when the illegal activity was publicly disclosed. *Id.* at 396-98. The Second Circuit held that these claims did not allege proximate cause because the decline in stock price was caused by public disclosure of the illegal scheme rather than the scheme itself, and because the shareholders were not the intended victims of the scheme. *Id.* at 400.

The district court concluded that Petitioners had failed to allege proximate cause for similar reasons. First, the court found that Petitioners themselves had alleged that the decline in the gambling companies' shares was caused by the government "crackdown" on online gambling rather than the funds' allegedly illegal investment in those companies. Pet. App. 13a. Second, the court found that investors in the funds, such as Petitioners, were not the intended victims or targets of the funds' allegedly illegal investments, but rather the intended beneficiaries. Pet. App. 14a. This placed them outside the scope of

those the underlying criminal statute, 18 U.S.C. § 1955, sought to protect.[1]

In a two-page summary order, the Second Circuit unanimously affirmed. Pet. App. 2a-5a. The court of appeals held that Petitioners had failed to allege proximate cause because "the decline in the funds' online gambling holdings was not the direct result of the RICO violation—the owning and/or financing of illegal gambling—but rather was the result of the subsequent 'government crackdown' on the illegal gambling." Pet. App. 4a.

REASONS FOR DENYING THE WRIT

The application of RICO's proximate cause requirement in the decision below does not raise any question warranting review by this Court. Petitioners fail to identify any conflict with this Court's precedent or split among the circuits. To the contrary, the Second Circuit's summary order is consistent with the holdings in *Bridge*, 128 S. Ct. 2131, *Holmes*, 503 U.S. 258, and *Hemi*, 130 S. Ct. 983 concerning RICO proximate cause. Nor is there any conflict among the circuits concerning the absence of proximate cause in this case. Further, the petition does not present an issue that is recurring or of national importance, but rather a novel, *sui generis* theory that seeks to invoke RICO to recover investment losses. In addition, this case is a poor vehicle in which to address RICO proximate cause, as there are

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[1] Because there were no federal claims remaining, the district court declined to exercise supplemental jurisdiction over Petitioners' state law claims Pet. App. 15a. Petitioners have since refiled their purported state law claims in Delaware Chancery Court. *Hartsel v Vanguard*, No. 5394 (filed Apr 7, 2010)

alternative grounds for affirming the decision below. The decision below was correct, in accord with years of precedent, and does not warrant this Court's attention.

I. THE DECISION BELOW DOES NOT CONFLICT WITH DECISIONS OF THIS COURT OR OTHER CIRCUITS.

A. There Is No Conflict With The Decisions Of This Court.

Although Petitioners contend that the decision below conflicts with this Court's decisions in *Bridge*, 128 S. Ct. 2131, *Holmes*, 503 U.S. 258, and *Hemi*, 130 S. Ct. 983, those cases did not involve the question presented here, and the decision below was consistent with their holdings.

1. The Second Circuit's decision does not conflict with this Court's holding in *Bridge*. Nothing in *Bridge* supports Petitioners' theory that alleged RICO violators can bring RICO claims when "contributing causes—including government action—had intervened" to put an end to the alleged RICO violations. Pet. 7-8.

In *Bridge*, a county held an annual public auction to sell tax liens on property of delinquent taxpayers. 128 S. Ct. at 2135. The bidding often produced ties, and the county allocated wins among tying bidders on a rotational basis. *Id.* To make the allocation fair, the county required that each bidder submit bids only in its own name. *Id.* The plaintiffs in *Bridge* were bidders who had received fewer parcels because defendants had illegally disguised their identities, by using agents, to acquire a disproportionate share of parcels. *Id.* at 2136.

The question before this Court in *Bridge* was whether a RICO claim could be based upon mail fraud without alleging first party reliance. *Id.* at 2137. *Bridge* did not address intervening cause (mentioning it only in passing, *id.* at 2144), because there was no intervening government action disrupting the predicate acts; the government action was routine administration of an auction. There was never any change in the government's action that led to plaintiffs' losses. As this Court recognized, there were "no independent factors that account for [plaintiffs'] injury." *Id.* Nothing suggests that if the plaintiffs in *Bridge* had been investors in the companies that submitted fraudulent bids, injured after the government took away their illicit wins, they would somehow have RICO claims.

2. Petitioners also contend that the decision below conflicts with this Court's decision in *Holmes*. Pet. 13-15. *Holmes*, however, did not consider whether RICO's proximate cause requirement could be satisfied by a decline in the value of an investment caused by a government crackdown on alleged predicate acts. Instead, it considered the much more basic question whether RICO incorporates a proximate cause requirement, and held that RICO requires a direct relation between the injury asserted and the predicate acts. *See* 503 U.S. at 265-70. In addition, in applying the proximate cause requirement, *Holmes* held that the chain of causation in that case was too attenuated because the plaintiff had alleged it was injured by a stock manipulation scheme that bankrupted two broker-dealers and in turn forced it to reimburse the broker-dealers' customers. *See id.* at 270-75.

Petitioners contend that the decision below conflicts with *Holmes* because the Second Circuit "refused to rely on [the *Holmes*] factors, dismissing them as nothing more than the 'underlying premises' of the proximate cause requirement." Pet. 15. But, as the decision below recognized, Pet. App. 5a, *Holmes* did not adopt a rigid three-factor test; it merely observed that a direct relation between the asserted injury and the alleged predicate act is required "for a variety of reasons." *Holmes*, 503 U.S. at 269. This Court has recognized that the factors identified in *Holmes* are "the directness requirement's *underlying premises*," using the exact same words Petitioners criticize the Second Circuit for using. *Anza v. Ideal Steel Supply Corp.*, 547 U.S. 451, 458 (2006) (emphasis added); *see also Bridge*, 128 S. Ct. at 2142 (noting that the factors support the "direct-relation requirement").

Petitioners' suggestion that review of the Second Circuit's summary order is necessary because it lacked a lengthy discussion of *Holmes* is unwarranted; if lack of lengthy discussion merited a grant of certiorari, every summary order would be a strong certiorari candidate. Moreover, there was no need for the Second Circuit to engage in detailed analysis of each *Holmes* factor, for its prior decisions rejecting similarly attenuated RICO claims had performed such analyses. The Second Circuit's citation to its prior cases, such as *American Express*, does not amount to applying a "mechanical rule." The Second Circuit analyzed Petitioners' RICO theory under prior precedents applying *Holmes*, and found that proximate cause could not be established.

3. There is also no conflict with *Hemi*. *Hemi* did not involve a government crackdown or an alleged

injury resulting from declines in a company's stock price. In that case, the City of New York sued a tobacco seller for failing to disclose customer information, which impeded the City's ability to collect sales tax from those customers. *See* 130 S. Ct. at 987-88 (plurality op.). Far from suggesting any conflict between *Hemi* and the decision below, Petitioners simply observe that *Hemi* involved an injury to a third party caused by a fourth party, rather than a "first step" injury, which they purport to assert here. Pet. 21. Petitioners themselves acknowledge that there is no binding determination in *Hemi* because of the lack of any agreement by a majority of the Court, Pet. 13 n.4, and none of the *Hemi* opinions suggested that all "first step" injuries (even if the allegations here somehow qualified) satisfy the proximate causation requirement. In *Hemi*, the plurality found that, "in the RICO context, the focus is on the directness of the relationship between the conduct and the harm." 130 S. Ct. at 991. The decision below does not conflict with any decision of this Court.

B. There Is No Conflict With Other Circuits.

Petitioners also argue that the decision below conflicts with the decisions of other circuits. Pet. 10-11, 21. They fail to show any conflict, however, because none of the cases they cite involved investors in an entity that was alleged to have owned an illegal enterprise or an injury caused by law enforcement.

Several cases cited by Petitioners found proximate cause on their particular facts but are inapposite. For example, two cases cited by Petitioners involved employees alleging that their employers engaged in "schemes to depress wages of legal workers by wide-

spread hiring of illegal workers." *Williams v. Mohawk Indus., Inc.*, 465 F.3d 1277, 1290 (11th Cir. 2006); *accord Trollinger v. Tyson Foods, Inc.*, 370 F.3d 602, 605 (6th Cir. 2004). These courts found proximate causation had been alleged because the employers' alleged scheme, unlike the investments here, had "the purpose and direct result" of hiring illegal aliens because they accepted low wages, thereby depressing the wages of legal workers. *See Williams*, 465 F.3d at 1289; *Trollinger*, 370 F.3d at 605, 618-19. Another case involved allegations that union negotiators agreed to costly concessions for their members, causing a direct injury in exchange for covert personal benefits. *See Cox v. Administrator U.S. Steel & Carnegie*, 17 F.3d 1386, 1392-93 (11th Cir. 1994). None of these cases involved intervening causes such as the "crackdown" alleged here. Rather, all involved direct injuries.

Other cases cited by Petitioners found proximate causation where, unlike here, the conduct at issue was targeted at the plaintiffs. For example, in *Mid Atlantic Telecom, Inc. v. Long Distance Servs. Inc.*, 18 F.3d 260 (4th Cir. 1994), a telecommunications company claimed that a competitor fraudulently added time to its bills so that it could present deceptively low rates and poach customers. *Id.* at 261. Because the telecommunications company allegedly was the "direct target" of the competitor's fraudulent scheme, the Fourth Circuit found proximate cause had been adequately alleged. *Id.* at 263-64; *see also Newcal Indus., Inc. v. Ikon Office Solution*, 513 F.3d 1038, 1055 (9th Cir. 2008) (finding that proximate cause allegations were sufficient where plaintiff alleged that competitor fraudulently extended lease agreements and service contracts with customers); *RWB Services, LLC v. Hartford Computer Group,*

Inc., 539 F.3d 681, 687-88 (7th Cir. 2008) (finding proximate cause allegations sufficient where plaintiff was allegedly "direct victim" of alleged scheme to fraudulently keep returned cameras and repackage as new). None of these cases involved situations, such as this one, where the plaintiffs were investors in the very entities that allegedly engaged in racketeering activity or where law enforcement had caused the alleged injuries.[2]

Finally, Petitioners allege there is a circuit split over the application of *Holmes*, noting that, unremarkably, cases from other circuits have considered the *Holmes* factors in determining proximate cause. Pet. 16. But there is no conflict, let alone a square one, between these cases and the decision below, because the Second Circuit cited cases showing that the *Holmes* factors do not support proximate cause under circumstances such as those here. Pet. App. 4a. Petitioners have yet to point to any decision in any circuit (or this Court) that permitted RICO claims to proceed where the injuries were caused by the interruption of the predicate acts, as alleged here.

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[2] Petitioners assert that two other court of appeals' decision conflict with the decision below, but neither of these decisions found the allegations of proximate cause were adequate. *See Oki Semiconductor Co v Wells Fargo Bank, Nat'l Ass'n*, 298 F.3d 768, 774 (9th Cir. 2002), *Steamfitters Local Union No. 420 Welfare Fund v. Philip Morris, Inc.*, 171 F 3d 912, 933 (3d Cir 1999)

II. THE PETITION DOES NOT PRESENT AN IMPORTANT AND RECURRING ISSUE, AND IS A POOR VEHICLE TO RESOLVE ANY RICO ISSUE.

The petition should also be denied because Petitioners present a novel RICO theory that is unlikely to recur and presents no issue of national importance. And this case is a poor vehicle for resolving questions about RICO proximate cause, because there are alternative grounds for affirming the judgment.

Petitioners have not shown that this case presents a recurring question. Citing a single newspaper article, they assert this case may affect the rights of individuals who invested in mutual funds that bought shares in publicly traded gambling companies. Pet. 12 n.3. However, they cite only two other cases in which RICO claims have been brought by such individuals, and they fail to disclose that petitioners' counsel represented the plaintiffs in both cases. *See* Civil Docket, *Wodka v. Causeway Capital Mgmt., LLC*, No. 09-cv-02625 (C.D. Cal.) (listing Hanly Conroy Bierstein Sheridan Fisher & Hayes, LLP as counsel for plaintiffs); Civil Docket, *Seidl v. Am. Century Cos., Inc.*, No. 08-cv-08857 (S.D.N.Y.) (same). Because Petitioners allege the "crackdown" on gambling companies occurred four years ago, any further claims would likely be time-barred. *See Agency Holding Corp. v. Malley-Duff & Assocs.*, 483 U.S. 143, 156 (1987) (four-year statute of limitations applies to civil RICO claims). Thus, far from a recurring, national issue, the theory presented in this case is the non-recurring brainchild of one set of plaintiffs' lawyers.

Contrary to Petitioners' suggestion, the decision below will not insulate mutual funds that make alle-

gedly improper investments. *See* Pet. 12. To the extent investors have a basis for pursuing claims, they could seek to assert state law claims for negligence, breach of fiduciary duty, and waste—the same theories Petitioners themselves have asserted, now in more than one court. *See supra* p.6 n.1.

Petitioners argue that certiorari should be granted to clarify confusion in the *Hemi* opinions concerning the role of foreseeability in RICO causation. Pet. 26. But Petitioners have not made any showing that this is an important or recurring issue. Even if it were, consideration of the alleged confusion about *Hemi* would be premature because *Hemi* was decided only months ago. Before its issues are revisited, *Hemi* should be given an opportunity to percolate in the lower courts, so that this Court has the benefit of their views on whether there really is any confusion and how to resolve it. The summary order below, decided before *Hemi*, provides no views on how *Hemi* should be applied.

In addition, this case would be a poor vehicle for revisiting any issues in *Hemi*, because there are alternative bases for the judgment: the failure to plead a predicate act and the failure of Petitioners to fall within the scope of the predicate act statute. Petitioners argued below, and argue here, that purchases of any amount of publicly traded shares of online gambling companies constitute "financing" or "owning" the companies in violation of 18 U.S.C. § 1955, which prohibits "financ[ing]" or "own[ing]" an illegal gambling business. Petitioners' expansive view of Section 1955 would make a felon out of anyone who purchases a minimal interest in a publicly owned gambling company, including passive investors, and even index funds. In the lower courts,

Petitioners did not cite any authority supporting this novel interpretation, nor did they point to a single investigation or prosecution of a public shareholder under Section 1955. Although the district court found it unnecessary to resolve this question in view of its decision for Respondents on the proximate cause issue, Petitioners' novel views of criminality are central to their complaint.

Petitioners' RICO theory also fails because their claims fall outside the scope of the statute on which they seek to rely. *See Hemi*, 130 S. Ct. at 994 (Ginsburg, J., concurring in part and concurring in the judgment) (rejecting claim "outside the scope of the very statute on which [the plaintiff] builds its RICO suit"); *Lerner v. Fleet Bank, N.A.*, 459 F.3d 273, 284 (2d Cir. 2006) ("When a plaintiff brings suit under RICO—as with any 'suit on a statute'—he or she must show both that he or she is within the class the statute sought to protect and that the harm done was one that the statute was meant to prevent."). Although Petitioners contend that the funds' investments ran afoul of a statute that prohibits owning or financing gambling companies (18 U.S.C. § 1955), they themselves stood to gain as beneficiaries while the alleged RICO violations were occurring uninterrupted. This puts them outside any class the statute seeks to protect. *See Lerner*, 459 F.3d at 284. Nor is the alleged "harm done"—a decrease in the value of investments in the allegedly criminal enterprise—the harm the criminal statute "sought to avoid." *Id.* Respondents briefed this issue below and the district court's opinion was based in part on its finding that Petitioners were not intended victims or targets of the alleged racketeering. Pet. App. 14a. Although the issue was not addressed in the Second Circuit's

summary decision, it too would provide adequate basis for affirming the dismissal below.

III. THE DECISION BELOW WAS CORRECT AND IN ACCORD WITH YEARS OF PRECEDENT.

Certiorari should also be denied because the Second Circuit was correct in summarily holding that Petitioners did not allege proximate cause.

To establish proximate cause under RICO, a plaintiff must show a direct causal connection between the alleged illegal predicate acts and the alleged injury. The RICO statute authorizes suits by persons injured "by reason of" a RICO violation. 18 U.S.C. § 1964(c). This provision incorporates the concept of proximate cause, *Holmes*, 503 U.S. at 265-68, and, in particular, a version of that concept requiring "some direct relation between the injury asserted and the injurious conduct alleged," *id.* at 268. The central question in applying RICO's proximate cause requirement is "whether the alleged violation led directly to the plaintiff's injuries." *Anza*, 547 U.S. at 461.

Petitioners failed to allege a direct causal connection. They did not allege that they were injured after the supposedly illegal stock purchases. Instead, they alleged that they were injured because state and local governments later commenced a crackdown on illegal gambling businesses, which included new federal legislation, and that "*[a]s a result*, the stock prices of all such illegal gambling businesses fell substantially." C.A. App. 32 (emphasis added). In their briefing before the district court, they further conceded that "the injury of which [Petitioners] complain (the loss in value of their mutual fund shares) flowed directly from the loss of illicit revenue suffered by

the unlawful gambling businesses when authorities stepped up enforcement of the criminal laws." C.A. App. 438. Given Petitioners' admissions that their alleged injuries were caused directly by law enforcement decisions, and particularly because such decisions are inherently discretionary, they could not allege the direct connection required to establish proximate cause under RICO. *Cf. Barts v. Joyner*, 865 F.2d 1187, 1195 (11th Cir. 1989) (holding that intervening decision of prosecutor to bring charges broke the chain of causation between the acts of the defendant officers and the defendant's prosecution); *Hand v. Gary*, 838 F.2d 1420, 1427-28 (5th Cir. 1988) (same).

This outcome is confirmed by the *Holmes* principles. The first principle, that "the less direct an injury is, the more difficult it becomes to ascertain the amount of a plaintiff's damages attributable to the violation, as distinct from other, independent, factors," 503 U.S. at 269, supports dismissal here because it would be impossible to determine what portion of the decline in a company's share price was attributable to an initial investment decision as opposed to an intervening "crackdown" or general market forces.

The second *Holmes* principle also supports dismissal, because Petitioners' novel RICO theory would require "courts to adopt complicated rules apportioning damages among plaintiffs removed at different levels of injury from the violative acts, to obviate the risk of multiple recoveries." *Id.* As the district court recognized, the direct victims of an illegal gambling operation are gamblers and competing, legal gambling businesses. Pet. App. 14a. Such victims are at a different "level[] of injury" from investors in alleged

owning/financing entities, such as Petitioners, who stood to gain from the success of allegedly illegal gambling operations and now claim injury because their investments turned out not to be profitable.

The third consideration set forth in *Holmes*, that "directly injured victims can generally be counted on to vindicate the law as private attorneys general," 503 U.S. at 269-70, also supports the outcome here. The more directly injured victims of illegal gambling enterprises, such as gamblers who used the enterprises and legitimate gambling businesses that competed with them, are in a position to bring suit if any RICO suits are needed. By contrast, investors such as Petitioners cannot be counted on to deter the alleged predicate acts because they stand to benefit from the alleged illegality until there is an intervening factor, such as the government "crackdown," that causes investment losses. And there is no need to extend the scope of RICO to encompass injuries traceable to law enforcement activity because the law enforcement activity itself will deter the underlying predicate act.

Finally, the decision below is correct under the reasoning of both the plurality and dissent in *Hemi*. In *Hemi*, the plurality found that, "in the RICO context, the focus is on the directness of the relationship between the conduct and the harm." 130 S. Ct. at 991. The "first step" in the chain of causation alleged by Petitioners was the funds' purchase of publicly traded shares in online gambling companies. Petitioners were not injured after this "first step." They only claim to have been injured after the government commenced a "crackdown," Congress adopted UIGEA, the online gambling companies withdrew from the U.S. market, and their share

prices declined. This is not a direct or "first step" injury.

The lower court's order also is correct under the dissent's reasoning. Justice Breyer maintained that proximate cause was established because "the harm is foreseeable; it is a consequence that Hemi intended, indeed desired; and it falls well within the set of risks that Congress sought to prevent." 130 S. Ct. at 997-98. Here, Petitioners have not alleged that the funds' losses were what the funds intended or desired, and losses incurred by investors in a gambling company are not within the risks Congress sought to prevent when it criminalized ownership of certain gambling companies. *See also id.* at 994 (Ginsburg, J., concurring in part and concurring in the judgment) (rejecting claim "outside the scope of the very statute on which [the plaintiff] builds its RICO suit").

The Second Circuit correctly held that proximate cause was not properly alleged in this case.

CONCLUSION

The petition for a writ of certiorari should be denied.

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IN THE

Supreme Court of the United States

DEANNA McBREARTY and MARYLYNN HARTSEL, individually, derivatively, and on behalf of all others similarly situated,

Petitioners,

v.

THE VANGUARD GROUP, INC., GEORGE U. SAUTER, DUANE F. KELLY, JOHN J. BRENNAN, CHARLES D. ELLIS, RAJIV L. GUPTA, AMY GUTMANN, JOANN HEFFERNAN HEISEN, ANDRE F. PEROLD, ALFRED M. RANKIN JR., J. LAWRENCE WILSON, ACADIAN ASSET MANAGEMENT, LLC, RONALD D. FRASHURE, JOHN R. CHISHOLM, BRIAN K. WOLAHAN, MARATHON ASSET MANAGEMENT, LLP, NEIL M. OSTRER, VANGUARD INTERNATIONAL EQUITY INDEX FUNDS, d/b/a VANGUARD EUROPEAN STOCK INDEX FUND, and VANGUARD HORIZON FUNDS, d/b/a VANGUARD GLOBAL EQUITY FUND,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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I. Reasonably Foreseeable Intervening Causes Do Not Insulate Racketeers from Civil Liability Under RICO

Respondents' own arguments demonstrate the urgent need for the Court to issue guidance concerning when intervening causes are sufficient to supersede a racketeer's liability under RICO. Respondents contend that Petitioners cannot satisfy proximate causation under RICO because their investment losses were the result of the law enforcement crackdown – and not Respondents' illegal investments – as if a RICO "chain of causation" could have only a single link. (Resp. Br. at 8, 16-17) To the contrary, Petitioners' losses were caused by both Respondents' illegal investments and the law enforcement crackdown. Had there been no crackdown, there might have been no losses. But had there been no illegal investments in the first place, there certainly would have been no losses.

By making the illegal investments, Respondents took a reasonably foreseeable risk that the mutual funds they managed would suffer losses if the government enforced the law. The illegal investments were therefore the primary and efficient cause of the losses, and law enforcement was merely a contributing cause. Law enforcement was not a superseding cause under RICO because it was part of the reasonably foreseeable risk that Respondents' racketeering created. *See, e.g., Bridge v. Phoenix Bond & Indem. Co.*, 553 U.S. 639, 128 S. Ct. 2131, 2144 (2008); *Hemi Group, LLC v. City of New York*, 130 S. Ct. 983, 998 (Jan. 25, 2010) (Breyer, *J.*, dissenting).

The caselaw, in both RICO and antitrust contexts, demonstrates that where, as here, wrongdoing is a material cause of injury, reasonably foreseeable contributing causes do not break the chain of causation. As Circuit Judge Straub observed in a majority opinion joined by then-Circuit Judge Sotomayor, "[a] contrary rule would effectively require that a plaintiff's injury be caused by only one source, and, as this is often not the case, it would operate to insulate from liability defendants who scheme with others in violation of RICO." *City of New York v. Smokes-Spirits.Com, Inc.*, 541 F.3d 425, 442-43 (2d Cir. 2008), *rev'd on other grounds*, 130 S. Ct. 983 (Jan. 25, 2010).

Respondents attempt to distinguish the Court's unanimous decision in *Bridge*, because, according to Respondents, *Bridge* "did not involve intervening causes." (Resp. Br. at 2) That is incorrect. In *Bridge*, the government, relying on the petitioners' misrepresentations, granted more liens to petitioners and fewer to respondents. The Court held that respondents' alleged injury – the loss of valuable liens – had been "the direct result" of petitioners' fraudulent representations to the government. The Court said, "[i]t was a foreseeable and natural consequence of petitioners' scheme to obtain more liens for themselves that other bidders would obtain fewer liens." 128 S. Ct. at 2144.

The Court explained that:

> the complete absence of reliance may prevent the plaintiff from establishing proximate cause. Thus, for example, if the [government] knew

> petitioners' attestations were false but nonetheless permitted them to participate in the auction, then arguably the [government's] actions would constitute an *intervening cause* breaking the chain of causation between petitioners' misrepresentations and respondents' injury.

Id. (emphasis added). Because the government had acted without knowledge of the fraud, however, its foreseeable actions in granting fewer liens to respondents did not even arguably break the chain of causation.

Thus, *Bridge* involved an intervening cause: the government's action in giving fewer liens to respondents. Like the present case, however, *Bridge* did *not* involve a *superseding* intervening cause because the government action had been the "foreseeable and natural consequence" of the defendants' wrongdoing.

Respondents do not dispute that the Court often looks to its antitrust proximate cause precedent for guidance in RICO cases. Nor do they deny that those cases confirm that reasonably foreseeable intervening events do not insulate wrongdoers from liability. Their brief nevertheless ignores those decisions.

Respondents implicitly concede that Petitioners have correctly stated the common law of superseding intervening causes.[1] They do not deny that the decision below is inconsistent with well-established common law

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1. Supreme Court Rule 15(2).

be absolved from liability merely because other causes have contributed to the result, since such causes, innumerable, are always present"). *Accord Blue Shield of Virginia v. McCready*, 457 U.S. 465, 480 n.17 (1982) (antitrust); *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 114 n. 9 (1969) (antitrust); *Williams v. Mohawk Indus., Inc.*, 465 F.3d 1277, 1288 n. 5 (11th Cir. 2006) (RICO); *Hasbrouck v. Texaco, Inc.*, 842 F.2d 1034, 1042-45 (9th Cir. 1987) (RICO).

Applying well-established common law rules concerning intervening causes, the courts have – without a single exception of which Petitioners are aware – consistently rejected efforts by negligent parties to evade liability on the basis that their wrongdoing was not the sole cause of harm. There is no good reason why racketeers should be treated with greater solicitude than parties who have merely been negligent. There is nothing in the language of RICO to hint of such a limitation.

Respondents acknowledge that *Hemi* fails to provide authoritative guidance to the lower courts because of the lack of a majority opinion. No good can come of Respondents' suggestion that *Hemi* be allowed to "percolate in the lower courts" (Resp. Br. at 14) before the Court resolves the conflict.[3] Further delay in resolving

3. Respondents apparently seek to invoke the Court's "practice of letting issues 'percolate' in the 50 States in the interests of federalism." *Johnson v. Texas*, 509 U.S. 350, 379 (1993) (O'Connor, J., dissenting). The interests of federalism have no application where, as here, the uniform interpretation of a federal statute like RICO is at issue. This practice should also not restrain the Court from resolving uncertainty surrounding an important issue for which the Court sought unsuccessfully to provide authoritative guidance.

these important questions will only benefit racketeers at the expense of victims as the statute of limitations expires on meritorious claims.

II. Courts May Not Disregard The *Holmes* Factors in Favor of a Mechanical Test

Respondents concede that other Circuits have held that proximate causation under RICO should be determined on a case-by-case basis using the *Holmes* factors. Respondents argue, however, that the decision below does not conflict with those decisions because the Second Circuit merely failed "to include in its summary order a detailed analysis" of the *Holmes* factors. (Resp. Br. at 2; *see id.* at 9) That is not a fair characterization of what the Court of Appeals did.

The Court of Appeals assumed for purposes of its decision that all three *Holmes* factors weigh in favor of a finding of proximate causation. Nevertheless, the Court of Appeals considered itself at liberty to disregard them, and to apply its own alternative black letter rule, to reach the opposite conclusion. This case does not present any issue whether the Court of Appeals correctly, albeit *sub silentio*, applied the *Holmes* factors. Rather, this case presents the question whether the Court of Appeals was free to ignore all three factors and rely on an alternative test based on *In re Am. Express Co. S'holder Litig.*, 39 F.3d 395 (2d Cir. 1994), that neither the Court nor any other Court of Appeals has ever approved or followed.

Implicitly recognizing that their first argument will not withstand scrutiny, Respondents argue that the *Holmes* factors weigh in their favor. (Resp. Br. at 17-18) They are wrong. If the *Holmes* factors weighed in Respondents' favor, the Court of Appeals would have simply said so and affirmed on that basis. The court did not do so because what this Court said in unanimously finding proximate causation in *Bridge* is equally true of this case:

> [H]ere, unlike in *Holmes* and *Anza*, [1] there are no independent factors that account for [Petitioners'] injury, [2] there is no risk of duplicative recoveries by plaintiffs removed at different levels of injury from the violation, and [3] no more immediate victim is better situated to sue. Indeed, [Petitioners and the Nominal Defendants whose interest they seek to represent] were the only parties injured by [Respondents' predicate acts].

Bridge, 128 S. Ct. at 2144.

Respondents contend that gamblers who lost money or legal gambling companies (as competitors) can be counted on to vindicate the law. However, gamblers and gambling companies suffered entirely separate injuries from the mutual funds. They do not have standing to seek redress for the injuries suffered by mutual funds and their investors. Moreover, while gamblers and competitors may claim to have been injured by the *operation* of the illegal gambling companies, they have not suffered more direct injury than Petitioners with respect to the relevant racketeering activity alleged in

the complaint: Respondents' investments in illegal gambling businesses in violation of 18 U.S.C. § 1955. Petitioners are the only parties who can be counted on to vindicate the rights of the mutual funds (and their investors).

Instead of applying *Holmes*, the Second Circuit applied a black-letter rule based on its 1994 decision in *American Express*. In that case, the court said that "the commission of the RICO violations was not what injured American Express. Rather, it was the *exposure* of those acts that caused the appellants' harm." 39 F.3d at 399-400 (emphasis added). The court below described *American Express* as extending to cases involving "exposure or *disclosure*" of predicate acts. (4a) (emphasis added)) Implicitly conceding that the injury here was the result of neither "exposure" nor "disclosure" of their racketeering, Respondents seek to expand the rule to cases involving "*interruption* of the predicate acts." (Resp. Br. at 12 (emphasis added)) Whether this ill-defined and ever-expanding rule applies to exposure, disclosure, or interruption of Respondents' racketeering, it has no application to this case.

A primary and recurring source of error in the lower courts' decisions, and in Respondents' brief, is a failure properly to identify the relevant racketeering activity alleged in the complaint. The racketeering predicate acts here are Respondents' investments in illegal gambling businesses in violation of § 1955. Respondents premise their arguments on the assumption that law enforcement "exposed" or "interrupted" their racketeering. (Resp. Br. at 7, 8 & 12) To the contrary, while the law enforcement that contributed to the

investment losses may have "interrupted" *the gambling companies'* illegal activities, it did not expose, disclose, or interrupt *Respondents'* racketeering.

The complaint does not allege that the share prices of the illegal gambling companies fell because Respondents' investments in them were somehow "exposed or disclosed." Nor does it allege that the stock prices fell because Respondents' racketeering activities were "interrupted." Rather, the complaint alleges that the stock prices of the gambling companies fell after U.S. law enforcement successfully choked off the gambling companies' source of illegal revenue. There is absolutely no relationship whatsoever between Petitioners' losses and any exposure, disclosure, or interruption of Respondents' predicate crimes.

Thus, Petitioners' complaint was dismissed on the basis of a bad rule that does not even apply.

III. The Injuries of Which Petitioners Complain Fall Within the Scope of the Predicate Statute

Respondents argue that Petitioners' injuries fall outside the scope of § 1955. (Resp. Br. at 15) That Respondents may have an alternative argument (which the Court of Appeals did not consider) is not a good reason to refuse review of the issues that the court below decided erroneously. The Court generally does not consider such alternative arguments where, as here, they are outside the scope of questions presented in the petition for certiorari and the Court of Appeals did not consider them. *See Roberts v. Galen of Va., Inc.*, 525 U.S. 249, 253-254 (1999) *(per curiam).*

In any event, Respondents' argument is unfounded. Section 1955, which prohibits ownership of "all or part of an illegal gambling business," was enacted together with RICO as part of the Organized Crime Control Act of 1970, Pub. L. 91-452, 84 Stat. 922 (the "OCCA"). The statement of findings that prefaces the OCCA expressly refers to "harm to innocent investors" and the corruption of "legitimate businesses" in connection with "syndicated gambling." 84 Stat. 922-923. Petitioners (innocent investors) and the mutual funds (legitimate businesses that Respondents corrupted) were harmed by Respondents' investments in illegal syndicated gambling. The injuries of which Petitioners complain thus fall well within the set of risks that Congress sought to prevent.

IV. There Is No Exception in § 1955 for Ownership of Illegal Gambling Businesses Whose Shares Are Traded on Foreign Exchanges

Respondents argue that passive, minority ownership of shares of illegal gambling businesses traded on a foreign stock exchange cannot possibly violate § 1955. (Resp. Br. at 14) Once again, the Court need not address this alternative argument because it is outside the scope of questions presented, and the Court of Appeals did not consider it.

In any event, Respondents' argument lacks merit. Section 1955(a) is clear and unambiguous. Whoever "owns all or part of an illegal gambling business" commits a felony. There is no exception for minority owners, passive owners, or illegal gambling businesses whose shares are traded on a foreign stock exchange. The Court should create no such exceptions.

In *Sanabria v. United States*, 437 U.S. 54, 70 n.26 (1978), the Court said, "[n]umerous cases have recognized that [§ 1955(a)] proscribes any degree of participation in an illegal gambling business, except participation as a mere bettor." The complaint here alleges that Respondents caused the mutual funds to participate in illegal gambling businesses as part owners – a form of participation expressly prohibited by the statute.

Respondents argue that ownership of minority interests ought to be exempted. (Resp. Br. at 14) This argument disregards the plain language of the statute, which prohibits owning "all or part" of an illegal gambling business.

Respondents contend that § 1955(a) should be read to exclude passive ownership. The terms "conducts", "manages", "supervises", and "directs" are sufficiently comprehensive to include all forms of active participation. By adding the terms "owns" and "finances" in the statute, Congress prohibited passive financial participation as well as active participation.

Respondents claim that Petitioners' view of Section 1955 "would make a felon out of anyone who purchases a minimal interest in a publicly owned gambling company . . . ." (Resp. Br. at 14) The flaw in Respondents' argument is that it ignores the *mens rea* requirement of § 1955(a). The crime of owning an illegal gambling business requires proof of criminal intent. *United States v. Ables*, 167 F.3d 1021, 1031 (6th Cir. 1999). Because of the *mens rea* requirement, Petitioners' interpretation of § 1955(a) poses no danger that innocent investors

will unwittingly be rendered felons. The complaint alleges that Respondents acted with knowledge that the off-shore gambling companies in which they invested millions of dollars of investors' money were flouting U.S. law.

Finally, the statute makes no exception for illegal gambling companies that trade on foreign stock exchanges. Respondents' proposed judicially created loophole would effectively legitimize off-shore havens for illegal conduct.

CONCLUSION

The Court should grant review.

Dated: May 17, 2010

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